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UNCLAS SANTO DOMINGO 003617

SIPDIS

SENSITIVE

DEPARTMENT FOR WHA/CAR AND EB/IFD/ODF
PLEASE PASS TO EX-IM BANK

E.O. 12958: N/A
TAGS: EFIN ECON DR
SUBJECT: GODR PUBLIC FINANCING STRAINED

¶1. (SBU) Central Bank Manager Apolinar Veloz told Econoff June 18 that GODR non-financial public sector finances are seriously off track from the IMF agreement for the first trimester of 2004. Veloz's remarks track with what Technical Secretary Carlos Despradel reported to the DCM June 1.

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Despradel had said that due to inadequate tracking of bilateral project-related loans by government credit agencies and government letters of credit drawn on GODR-owned Banco de Reservas (BanReservas), the government had accumulated significantly more debt than it had reported while negotiating the IMF agreement. Veloz reaffirmed that President Mejia has frozen all project loans in an effort to get government expenditures back on track.

¶2. (SBU) According to Veloz, non-financial public sector debt cannot increase if the GODR is to meet the IMF targets, but added that BanReservas and other banks have steadily increased their lending to the GODR. Veloz said that the Monetary Board on June 17 approved his initiative to immediately stop all lending to the government by BanReservas and other commercial banks.

¶3. (SBU) Central Bank statistics show that not counting off-budget "residuals," non financial public sector expenditures exceeded programmed amounts by 6.4 billion pesos ($135 million). In addition, Veloz explained that the GODR had spent five billion pesos on the electricity sector and an additional 1.5 billion pesos on propane gas subsidies that was off-budget. There was also non-explained residual expenditures of more than 2 billion pesos. In total, including current expenditures, capital expenditures and residual, the GODR overspent nearly 9 billion pesos ($187.5) during the first trimester. Veloz estimated that the consolidated deficit would be about four percent of GDP.

¶4. (SBU) Both the current PRD government and the incoming Fernandez administration recognize the urgency of the fiscal imbalance and are now working together on possible fiscal reform measures. They have met jointly with the IMF on at least two occasions and debt sustainability was reportedly a key point in those discussions.

¶5. (SBU) Debt presents a looming problem. The Paris Club agreement to reschedule nearly $200 million in bilateral debt (plus $120 million in GODR debt to the private sector) could unravel if the GODR is not on track with the Fund. None of the analysis takes into account the internal arrears owed to the electricity sector that reportedly total some $450 million. Veloz would not speculate on a total figure for the electricity sector, admitting that it was a "black hole." Nor does it include the quasi-fiscal deficit of nearly 80 billion pesos the Central Bank holds in certificates of deposit. Moreover those certificates carry a weighted average interest rate of about 40 percent, according to Veloz, and make it extremely difficult to meet the Fund program's monetary target.

¶6. (SBU) The practical effect of the GODR's financial woes is being felt first in the electrical sector. This week, the country is producing less than 60 percent of demand due to plant shut downs over non-payment. The Embassy also has reports of U.S. companies not being paid for government contracts. One such case involves a water project reportedly backed by EX-IM Bank guarantees. There are also reports of the Army not being able to purchase fuel for its vehicles or helicopters, and the Navy unable to purchase fuel or perform routine maintenance on its boats.

¶7. (SBU) Comment: In light of the financial uncertainty and USG interest in the GODR getting back on track with the IMF program, Embassy recommends that the USG postpone further consideration of bilateral lending for procurement or infrastructure projects. Moving forward with such proposals sends conflicting messages to the GODR and puts the government at increased risk of default. Moreover, new loans at this time may not reflect the priorities of the new administration that will be inaugurated August 16, and may not be within the framework of a fiscal reform package.

KUBISKE